IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

HEALTHSOUTH CORPORATION, et al.,

Plaintiffs,

v.

MID-PENINSULA ENDOSCOPY ASSOCIATES, INC., et al.,

Defendants
_____/

No. C 06-01911 CRB

MEMORANDUM AND ORDER

Plaintiffs filed this state law breach of contract action in federal court. Now pending before the Court is defendants' motion to dismiss (1) for lack of diversity jurisdiction, and (2) for failure to state a claim. After carefully considering the papers filed by the parties, the Court concludes that oral argument is unnecessary, see Local Rule 7-1(b), and GRANTS defendants' motion to dismiss.

ALLEGATIONS OF THE COMPLAINT

This dispute involves the operation of the San Mateo Endoscopy Center ("the Center"), a state licensed ambulatory outpatient surgical center providing endoscopy services. Complaint ¶ 11. The Center is operated pursuant to a Limited Partnership Agreement. Defendant Mid-Peninsula Endoscopy Center ("MPEC") is the General Partner and defendant Mid-Peninsula Endoscopy Associates, Inc. and plaintiff Endoscopy Center Affiliates, Inc. ("ECA") are the only two limited partners. Id. ¶ 12-13.

The Limited Partnership Agreement and a General Partnership Agreement that governs MPEC require plaintiff ECA "to provide certain enumerated services to the Center in its role as Manager." Id. ¶ 17. Since 1994, ECA and its corporate affiliate, plaintiff Healthsouth, "have been providing services to and incurring expenses on behalf of the Center in accordance with ECA's role as manager of the Center." Id. ¶ 18. For July and August 2005, defendants only made partial payments on the invoices for ECA's services, and defendants have made no payments for those services for September 2005 through December 2005. Id. ¶ 21. As of the filing of the complaint, defendants owe $900,000 for payment of ECA's manager services. Id. ¶ 22.

The Center purported to terminate ECA's role as manager of the Center as of December 12, 2005. Id. ¶ 26.

ECA and Healthsouth responded by filing this state-law diversity jurisdiction lawsuit in federal court. They make claims for breach of contract, breach of the implied covenant of good faith and fair dealing, quantum meruit, money had and received, money paid, promissory estoppel arising from defendants failure to pay ECA for the services it rendered to the Center as manager. They also allege that defendants failed to get adequate insurance for the Center, and that they failed to make partnership distributions to ECA.

DISCUSSION

Defendants now move to dismiss the complaint on the ground that the parties are not completely diverse and therefore the Court lacks subject matter jurisdiction. In the alternative, they move to dismiss certain claims for failure to state a claim.

I. Subject Matter Jurisdiction

A. Legal standard

Although defendants are moving to dismiss the complaint, *plaintiffs* bear the burden of proving that this Court has jurisdiction to decide this action. See Kokkonen v. Guardian Life Ins. Co. of America, 511 U.S. 375, 377 (1994) ("Federal courts are courts of limited jurisdiction. . . . It is to be presumed that a cause lies outside this limited jurisdiction, and the burden of establishing the contrary rests upon the party asserting jurisdiction.") (citations

omitted). "A plaintiff suing in a federal court must show in his pleading, affirmatively and distinctly, the existence of whatever is essential to federal jurisdiction, and, if he does not do so, the court, on having the defect called to its attention or on discovering the same, must dismiss the case, unless the defect be corrected by amendment." Tosco Corp. v. Communities for a Better Environment, 236 F.3d 495, 499 (9th Cir. 2001) (quoting Smith v. McCullough, 270 U.S. 456, 459 (1926)).

Moreover, "[f]or motions to dismiss under Rule 12(b)(1), unlike a motion under Rule 12(b)(6), the moving party may submit affidavits or any other evidence properly before the court. . . . It then becomes necessary for the party opposing the motion to present affidavits or any other evidence necessary to satisfy its burden of establishing that the court, in fact, possesses subject matter jurisdiction." Association of American Medical Colleges v. U.S., 217 F.3d 770, 778 (9th Cir. 2000).

B. Analysis

Defendants contend the Court lacks diversity jurisdiction because plaintiff ECA is a citizen of California, as are all the defendants. A federal court lacks diversity jurisdiction if any defendant is a citizen of the same state as any plaintiff. See Tosco Corp., 236 F.3d at 499. A corporation is deemed a citizen of any state in which it has been incorporated and of the state where it has its principal place of business. 28 U.S.C. § 1332(c)(1); id.

> Federal courts generally use one of two tests to determine a corporation's principal place of business. First, the place of operations test" locates a corporation's principal place of business in the state which "contains a substantial predominance of corporate operations." . . . Second, the "nerve center test" locates a corporation's principal place of business in the state where the majority of its executive and administrative functions are performed. . . . [W]here a majority of a corporation's business activity takes place in one state, that state is the corporation's principal place of business, even if the corporate headquarters are located in a different state. *The "nerve center" test should be used only when no state contains a substantial predominance of the corporation's business activities.* Thus, the Ninth Circuit applies the place of operations test unless the plaintiff shows that its activities do not substantially predominate in any one state.

Tosco, 236 F.3d at 500. Courts look to a number of factors "to determine if a given state contains a substantial predominance of corporate activity, including the location of

employees, tangible property, production activities, sources of income, and where sales take place." Id.

Defendants contend that ECA was a California corporation at the time it entered into the partnership agreement, upon which now it bases its lawsuit, and, in any event, ECA's only business is the operation of the Center in California.

Plaintiffs respond by offering evidence that ECA has been merged into several other corporations (most of which were also California corporations), and the entity that emerged is registered as a Delaware corporation. They also argue that the nerve center, rather than place of operations, test applies because ECA does not conduct any business at all; instead, they characterize it as a "passive investment vehicle" whose "sole function is to act as an owner of investments in partnerships that operate endoscopy centers." Declaration of Shawn Patzkowsky (Patzkowsky Decl.) ¶ 8. Since "virtually all" of ECA's corporate activity occurs in Alabama, under the nerve center test Alabama, rather than California, is ECA's principal place of business.

Plaintiffs have not met their burden of proving that ECA is not a citizen of California. Plaintiffs argument ignores the nature of this lawsuit, the allegations of their complaint, and the partnership agreements: this lawsuit arises from ECA's business activities in California. ECA seeks to recover over $900,000 it claims it is entitled to as reimbursement for *business services it provided to the Center in California* as manager of the Center. Complaint ¶¶ 17-22. If ECA were merely a "passive investment vehicle" it could not bring a lawsuit for reimbursement of expenses it incurred operating a California endoscopy center.

ECA has offered evidence that more than 60 percent of its revenue is derived from California. ECA does not distinguish between revenue from managing endoscopy centers and revenue as an investor; as the burden is on plaintiffs to prove jurisdiction, the Court will assume that the revenue is derived primarily from operating the Center. Plaintiffs do not offer any evidence to the contrary.

ECA's reliance on Vareka Investments, N.V. v. American Investment Properties, Inc., 724 F.2d 907 (11th Cir. 1984) as an "analogous situation," Opposition at 7, is misplaced. In

Vareka, the plaintiff "passive investment vehicle" merely invested in real estate in Florida. The trial court specifically found that the plaintiff was not involved in the day-to-day operation of the real estate at issue, and did not "take any other action which might be construed as operating or managing the property." Here, in contrast, ECA alleges that it operated and managed the Center; indeed, its lawsuit is premised on its assertion that defendants have failed to pay ECA for its operation and management of the Center. The partnership agreements upon which ECA bases its lawsuit require ECA to operate the Center. As such business activity appears to be the only activity in which ECA engages, or at least it is the only activity of which there is evidence in the record, a substantial predominance of ECA's business activities occur in California and therefore ECA is a California citizen for purposes of diversity jurisdiction.

CONCLUSION

As plaintiffs have not met their burden of proving that there is complete diversity, defendants' motion to dismiss for lack of subject matter jurisdiction is GRANTED.

IT IS SO ORDERED.

Dated: June 2, 2006

CHARLES R. BREYER
UNITED STATES DISTRICT JUDGE